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RUCPDOC/DEPT OF COMMERCE WASHDC

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SENSITIVE

SIPDIS

STATE FOR EUR/WE, EEB/IFD/OMA

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ENERGY FOR PIA/K.BALLOU

TREASURY FOR OIA/OEE/T.O'KEEFFE,D.WRIGHT

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Bank Restructuring Fund Approved

1.(U) The Council of Ministers approved on June 26 a Royal Decree-Law creating a nine-billion euro Orderly Bank Restructuring Fund (FROB) aimed primarily at addressing expected solvency problems in savings banks (cajas). The GOS, first preference will be for troubled institutions to find private solutions such as raising capital or merging. The second option will be for institutions to use deposit guarantee funds. The last option will be restructuring with use of the FROB. The decree-law sets out a process through which troubled banks must submit business plans to the Bank of Spain. The fund will be able to issue debt for up to 27 billion euros during 2009. Of the initial nine billion euros, 6.75 billion will be funded by the GOS, using leftover funds from the Financial Asset Acquisition Fund created last fall to purchase bank debt, and 2.25 billion will come by the three existing deposit guarantee funds, which are funded by the banks and cajas themselves.

2.(SBU) Comment: Second Vice President and Economy/Finance Minister Elena Salgado told reporters after the announcement of the Decree-Law that the GOS would not seek to change the Cajas Law this year. Critics say the politicization of many cajas has contributed to their difficulties. Earlier this year, changes to reduce regional governments' control over cajas had been considered likely, but President Zapatero was reportedly lobbied on the issue by the Socialist presidents of Andalucia and Catalonia. This means that regional governments will continue to be able to block mergers of cajas across regional borders. Although the GOS had sought consensus and negotiated with the opposition Partido Popular for several weeks during the process of drafting the Decree-Law, initial PP reaction was to criticize the measure as insufficient. (Presidency announcement, 6/26; El Confidencial, 6/26; Expansion, 6/26)

OECD predicts GDP to Shrink 4.25% This Year

3.(U) The OECD issued on June 24 predictions for the Spanish economy that are somewhat more pessimistic than GOS predictions from earlier this month. It expects a 4.25% GDP contraction this year and an 0.9% contraction in 2010, when

it expects unemployment to reach almost 20%. The OECD also expects the budget deficit to approach 10% of GDP in 2010. The most recent GOS prediction had the economy shrinking 3.6% this year and 0.3% in 2010. (Europa Press, 6/24)

Record GOS Debt Issuances Expected

4.(U) The GOS will be forced to issue 100B Euros in debt this year to cover its budget deficit. Some analysts predict that public debt will account for 66% of GDP by 2010, compared to under 40% just a few years ago. There was high demand for Spain's first 50B Euros of bond issuances this year, but the GOS may find less demand -- and so have to pay higher interest rates -- for the remainder, as the worldwide bond market has become saturated. (El Confidencial, 6/22)

Tourism Slumps, Expected to Begin Rebound by End-2009

5.(U) The tourism industry, which accounts for 11% of Spanish GDP, is taking a hit in the economic crisis, with the number of foreign tourists in January-May 11.8% below the January-May 2008 level. This brings the number of foreign tourists to a 5-year low. Hotel nights booked fell 10.2% in the same period, and rates fell 5.3%. The decline was less than the 30% that some had anticipated, and the tourism industry is expected to begin rebounding by the end of 2009. (El Pais, 6/23; El Confidencial, 6/23)

CHACON